

# Joint Economic Committee WEEKLY ECONOMIC DIGEST

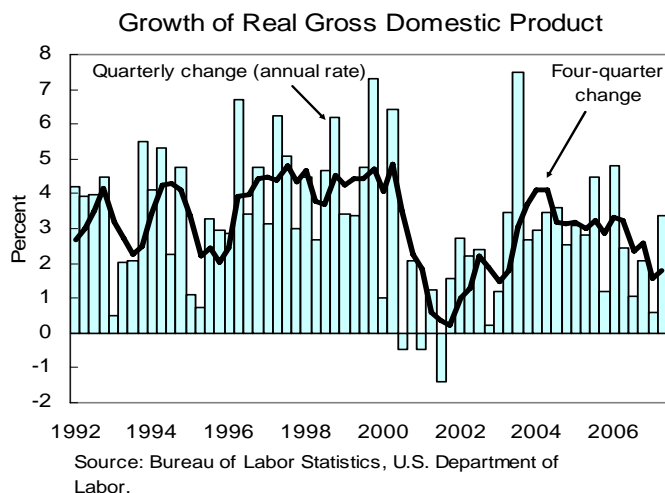
Senator Charles Schumer, Chairman  
Congresswoman Carolyn Maloney, Vice Chair

July 31, 2007

## ECONOMIC NEWS

### Despite Q2 Rebound, Growth Trends Remain Weak

**Economic growth rebounded in the second quarter.** Real (inflation-adjusted) gross domestic product (GDP) grew at an annual rate of 3.4 percent in the second quarter, following a 0.6 percent advance in the first quarter. The second-quarter acceleration was widely anticipated and largely reflects upturns in demands that were unusually weak in the first quarter such as net exports of goods and services, federal defense spending, and inventory accumulation. Even so, growth over the past year remains a relatively slow 1.8 percent (see chart). Most forecasters expect the economy to grow more slowly than the second-quarter's pace through the remainder of the year.



**Home sales were surprisingly weak in June.** Sales of new single-family homes declined by 6.6 percent to 834 thousand units at an annual rate last month. That drop was considerably larger than the 1.6 percent drop analysts had expected and it left new home sales 22.3 percent below last year's level. Sales of existing single-family homes also declined in June, dropping 3.5 percent to 5.0 million units (annual rate). That is 12.1 percent below last year's sales.

**Growth in capital spending by businesses remains weak.** Real (inflation-adjusted) business investment in equipment and software grew at a relatively weak 2.3 percent rate in the second quarter. Over the last four quarters, investment has risen by only 0.1 percent. In June, new orders for nondefense capital goods excluding aircraft—an indicator of future capital spending by businesses—declined by 0.7 percent. New orders have fallen by 2.4 percent over the past 12 months.

## IN FOCUS

### Reassessing a Weak Expansion

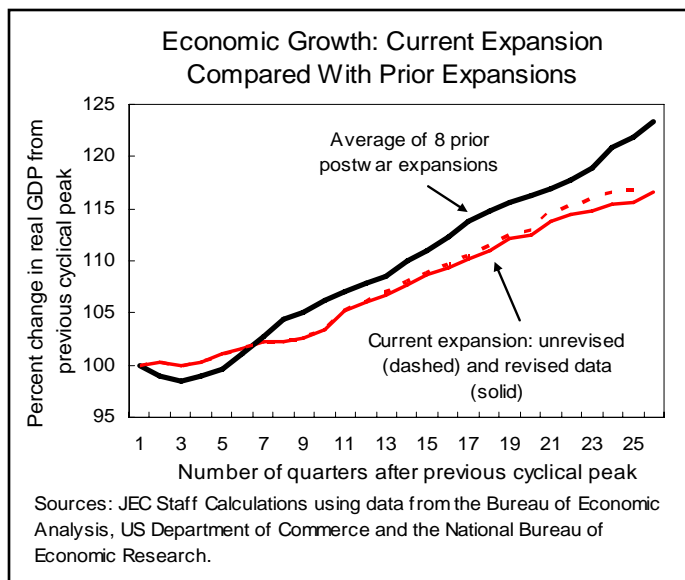
Last week, the Bureau of Economic Analysis (BEA) released its annual revisions to historical growth rates. The annual revisions allow BEA to incorporate new data and procedures that improve the accuracy of the national accounts. This year's revisions had the effect of slowing the growth rate of real GDP in recent years. As a result, the current expansion is now the weakest of all the economic expansions since the end of World War II.

The second quarter of this year marked the 25th quarter since the first quarter of 2001 (the previous peak in the business cycle as determined by the National Bureau of Economic Research). Over those 25 quarters, real GDP has grown by 16.5 percent, somewhat below the growth indicated by the data prior to the revisions, and well below the economy's average 23.3 percent growth at the same point in previous postwar expansions (see Snapshot). That translates into an average annual rate of expansion of 2.5 thus far in the current expansion, as compared with a 3.4 percent average pace in prior expansions.

Business cycles are idiosyncratic and that fact complicates any comparison of growth paths across different cycles. In recent decades, for example, cycles have become less frequent and economic expansions have tended to last longer than they did in the early decades after World War II.

*Continued on reverse...*

## SNAPSHOT



# Joint Economic Committee WEEKLY ECONOMIC DIGEST

## THE WEEK AHEAD

### DAY

### RELEASE

**Tuesday 31**

Personal Income and Outlays (June 2007) and Revisions (January 2004-May 2007)  
Employment Cost Index (June 2007)  
Construction Spending (June 2007)

**Thursday 2**

Full Report on Manufacturers' Shipments, Inventories and Orders (June 2007)

**Friday 3**

The Employment Situation (July 2007)

*Friday,  
August 3rd:  
July jobs report*

## THE ECONOMY AT A GLANCE

KEY INDICATORS	MONTH			QUARTER			YEAR	
	June	May	Apr	2007 Q2	2007 Q1	2006 Q4	2006	2005
Real GDP Growth (%)	—	—	—	3.4	0.6	2.1	2.9	3.1
Unemployment (% of labor force)	4.5	4.5	4.5	4.5	4.5	4.5	4.6	5.1
Labor Productivity Growth (%)	—	—	—	n.a.	1.0	2.1	1.6	2.1
Labor Compensation Growth (%)	—	—	—	n.a.	3.2	3.6	3.1	3.3
CPI-U Inflation (%)	2.3	8.4	5.1	6.0	3.8	-2.1	3.2	3.4
Core CPI-U Inflation (%)	2.8	1.8	2.1	1.9	2.3	1.9	2.5	2.2

Sources: Bureau of Economic Analysis, U.S. Department of Commerce; Bureau of Labor Statistics, Department of Labor.

Notes: Except where otherwise noted, values in the table represent percent changes at seasonally adjusted annual rates. Productivity is output per hour worked in private nonfarm businesses. The Employment Cost Index is for civilian workers in government and business. Core CPI-U inflation is the percent change in the CPI-U excluding food and energy as reported by the Bureau of Labor Statistics. The designation "n.a." denotes that data are not yet available.

## IN FOCUS (Continued)

Even so, the current pace of expansion (2.5 percent at an annual rate) is lower than the growth posted in either of the two most recent expansions. Twenty-five quarters into the expansion that began in the third quarter of 1990, real GDP had grown at an average annual pace of 2.8 percent. At the same point in the expansion that began in the first quarter of 1980, the economy had grown at an average annual rate of 2.9 percent.

What accounts for the relatively slow rate of the current expansion? The single-most significant difference between this expansion and its predecessors is the current weakness of investment spending. Since the first quarter of 2001, gross domestic private investment has increased at a 1.5 percent average annual rate. That pace is well below the 4.1 percent average rate of investment growth in the first 25 quarters of previous expansions; It's well below the 5.8 percent pace at the same point in the 1990s expansion; and it's well below the 3.2 percent rate in the 1980s expansion. In fact, investment growth in the current expansion has been the weakest of all expansions since World War II.

Because the period since 2001 includes both the housing boom as well as the slump, the weakness in housing since 2005 is only a small part of the investment weakness over the longer period. In contrast, capital spending by businesses on equipment and software (well over half of total investment spending) accounts for a significant portion of the weakness in the current investment expansion relative to previous experiences. Since 2001, spending on equipment and software has grown at a 2.1 percent average annual rate. That's below the average 4.8 percent pace for all previous expansions and only a fraction of the 8.8 percent average annual pace at the same point in the 1990s expansion. With profits unusually high and capital costs relatively low, the investment weakness is something of a mystery to economists.

The Administration has touted its tax cuts as having boosted growth by encouraging investment. In fact, both overall growth and business investment have been relatively weak during this expansion. In the second quarter of this year, business investment in equipment and software was only 0.1 percent above last year's level and remains a risk to the near-term outlook.